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Economic Conditions
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General Business Conditions

THE interest of the country, as the season advances and fighting spreads on new fronts, is centered intensely on the military news. In the early part of the past month there appeared to be more ground for optimism than at any time since Pearl Harbor. The defeats inflicted on the Japanese in the Coral Sea and off Midway were the more heartening because they were achieved through air power, in which the United States will be supreme; and sentiment was likewise lifted by the gigantic British air raids on German cities. In the business situation the feeling was reflected in higher stock prices. Also, talk was heard of an earlier end of the war than previously expected,—a prospect which if supported by later developments would naturally lead to modification of business policies, in anticipation. There is evidence that merchants particularly, reviewing their heavy inventories, were beginning for the first time to take post-war conditions into current calculations.

"UNITED WE STAND"

Against this news the defeat of the British in Libya, the grave danger to the Middle East, and the unabated ship sinkings by submarines, have come as profound disappointments; and the near future may bring other causes of anxiety and strain. It is to be expected that the Germans will make a supreme effort, before the forces of the United States are fully in the field, to fortify themselves with new strategic positions and new supplies of raw materials, and if possible to end the war on the Eastern front so that they may be prepared for it on the West. If they have any hope of winning the war, this is obviously the time to do it.

Until the German attacks of this Summer have been met and sustained, estimates of the length of the war are premature. It is true that the United States has the strength to throw the balance heavily in favor of the United Nations, but only when that strength can be fully exerted on the battlefield. Our production is becoming stupendous, but we are learning the difficulties of speedily transporting arms and supplies to the places where they are most needed, all in the proper proportions for an effective effort.

It is doubtless also true that if the German armies fail to win major victories, before next Winter, the German people will experience bitter disappointment and loss of morale; for they know that the United States will become a constantly stronger foe, and the possibility of ultimate victory will become more and more remote. On the other hand, German victories that crushed Allied forces or secured new raw materials this Summer would prolong the war and increase immeasurably its cost in money and lives.

Growth of Production

During the past month the Administration has revealed more information on war production than has been made public since we entered the war. There seems little reason why the figures should ever be suppressed, for they must be as disheartening to the Axis as they are encouraging to the United Nations. President Roosevelt has said that in May nearly 4,000 airplanes were produced, more than 1,500 tanks, nearly 2,000 artillery pieces and anti-tank guns exclusive of anti-aircraft and tank equipment, and over 50,000 machine guns and 50,000 sub-machine guns. In 1918, four years after the beginning of the war and a year and a half after our entry, the peak machine gun production in any month was 35,000 and the peak in complete field artillery units was 420.

Machine tool output, which has made this production possible, reached $107 millions in the month of May; this figure equals the output in many full years before the war and compares with a total of $185 millions in 1929.

These records, and the far greater ones to come, may be credited largely to unprecedented advances in manufacturing methods, efficiency in plant operation by both management and labor, and corresponding reduction in the man-hours required per unit of output. No greater demonstration of the effectiveness and productive capacity of the American enterprise system has ever been given. The armaments are the product of millions of working men and of thousands of plants, guided by their own engineers and management, and supported by a capital investment, the purpose of which is to cut costs and increase output. Mr. Nelson paid indirect tribute to all elements in production, when before a Senate Committee on June 25 he said in effect that present plants were cutting up so much metal, and were so draining the supplies of raw materials, that fewer plants would be built than originally thought to be needed.

The country is benefitting from the efficiency of its productive system in more ways than may be realized. Not only does it make the war effort effective and cut costs, but the saving of man-hours reduces labor requirements and postpones the time of labor shortage, thus raising the ceiling on potential output. Mr. Ernest Kanzler, chief of the automotive branch of the War Production Board, has stated that first estimates of the number of men required for war work in the Detroit area can now be reduced by 25 to 30 per cent. With this reduction the employment peak will still be far higher than in peacetime, but it substantially diminishes the difficulties of labor supply, housing and local transportation.

The production accomplishment is itself the best answer to charges of waste and ineffectiveness, made by critics of industrial management or of the industrial system.

Cost-Plus-Fixed-Fee Contracts

The proposal in Congress to prohibit further cost-plus-fixed-fee contracts grows out of charges, based on isolated instances, that the arms program is being achieved at exorbitant costs. Actually, the cost-plus-fixed-fee contracts were devised for the protection of the Government as well as of manufacturers. In taking orders for delivery stretching in many cases years ahead, and for things which they had never made before, the industries could not accurately foretell their costs. They could not be expected to assume long-term fixed price contracts, at the risk of grave losses if costs rose, unless prices were set at levels to cover all contingencies. Such prices might well prove exorbitant. The cost-plus-fixed-fee contract was devised to treat both parties fairly.

Probably some persons confuse these contracts with the "cost plus" contracts of the first World War, under which the contractors received a percentage on cost and therefore had more financial interest in letting costs go up than in keeping them down. In fact, the present contract is a different instrument, designed to avoid the mistakes in the last war. While details of contracts vary considerably, the basic principle is that the contractor receives a fixed fee calculated as a percentage of a base cost. If costs rise above the base the Government reimburses him only for the added cost. If costs drop below the base the Government benefits; in some cases the contractor is allowed a small percentage of the saving as an inducement to efficiency.

In carrying out the contract the costs which are admissible are carefully defined by government regulations. They do not include interest on invested or borrowed capital, nor many other items which are part of overhead costs. Because of these provisions the true return to the manufacturer is necessarily less than the fixed fee allowed him. The fees of course are subject to the corporate income and excess profits taxes. Advertising and selling expenses are in general inadmissible, and the Government can limit allowances for officers' and employes' compensation when the circumstances warrant.

On the evidence, the Government has adequate powers to prevent abuses of the contracts. To prohibit them, because abuses are alleged or have occurred in some cases, would be to disregard the compelling reasons why the contract was adopted, to throw the situation again into confusion, and to set back the war effort.

There is no perfect way to handle this gigantic productive effort. Any method employed must be compared with the possible alternatives. The cost-plus-fixed-fee contract has weaknesses, but in industrial operations especially it is in general more workable and equitable than other forms; it is more acceptable as a basis both for bank credit and for progress payments by the Government than other contracts; and under it the costs of producing many war products have been steadily and substantially reduced. The problem is not so much one of the particular form of contract as of the competence and experience of both the contractors and the government agencies.

Slackening in Distributive Trade

In domestic business the chief interest has been in distributive trade. In the early months of this year sales of department stores, chain stores and mail order houses were of record size, 20 to 30 per cent above a year earlier.

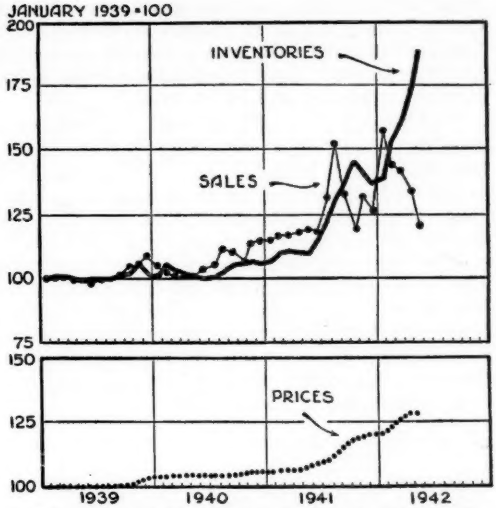
During much of the past two months, however, sales have been below or no better than last year; and as merchandise prices average some 17 per cent higher, each dollar of sales represents a smaller physical volume.

There are several reasons for this slackening. Consumers, like merchants and manufacturers, had been buying ahead in anticipation of scarcities and higher prices. They were well-stocked when the overall price ceilings were announced at the end of April, and the ceilings removed much of the inducement to forward buying. Moreover, installment and open credit terms have been tightened, and sales of durable goods are smaller because of shortages. These appear to be the principal explanations for sales declines.

Obviously buying power is not lacking. To be sure, some groups of the population and some areas have lost purchasing power due to higher taxes, higher living costs and industrial dislocations; and people are saving to buy war bonds. But aggregate income payments have increased steadily. According to the latest figures of the Department of Commerce, national income in April was at the rate of $109 billions annually. With this money in the hands of the public, consumption will hardly decline except as an effect of scarcities and rationing. There is an obvious contradiction between expectations of poor retail trade, so far as goods can be had, and fears of inflation.

With sales taking this turn, wholesale prices also ceilinged, and with the hope of a shortened war already referred to, both retailers and wholesalers have slowed down their buying. Moreover, they are on notice that the War Production Board may limit inventories which larger distributors may carry. Retail commitments were extremely heavy early this year, and department store inventories at the end of May were 70 per cent larger than a year ago. The accompanying chart diagrams indexes of department store sales and inventories, and gives the course of prices, from which the influence of higher prices on the sales and inventory figures may be judged. The chart shows that during the past three months a sharp rise has taken place in the ratio of inventories to sales. When inventories climb at this rate they almost inevitably become unbalanced, including surpluses of items which prove less saleable than expected.

The business situation will be all the sounder for a turn to more conservative buying. No criticism can be offered of merchants individually for building up inventories, for their function is to have goods to sell, and part of their present stocks cannot be replaced during the war. Nevertheless, the accumulation has given an appearance of shortage of certain materials and manufactured goods which in fact did not exist; and its continuation, past the time when new plants and equipment make it possible



Department Store Sales, Inventories, Prices
(Sales and Inventories, Indexes of Federal Reserve Board: Prices, Fairchild Price Index)

to use more labor in war work, would be at the expense of the war effort. Moreover, the inventory buying has forced up prices and contributed to inflationary influences. Within the past month Chairman Eccles of the Federal Reserve Board, in a letter concurred in by the heads of other government agencies, has asked banks and financing institutions to discourage all abnormal purchases of civilian goods and to scrutinize every application for credit for that purpose. From the merchant's standpoint heavy inventories involve obvious hazards, familiar to those who remember 1920 and even 1933-34 and 1937.

Effects of War on Distribution

The probable effects of the war and the price ceilings upon retailing have steadily become clearer. The volume of sales of durable goods stores—including automobiles, household furnishings, building materials and hardware, and jewelry—has declined some 40 per cent from the 1941 peak, according to an index compiled by the Department of Commerce, and is rapidly approaching the low level of 1938. Reduced supplies of durable goods will also curtail volume in general stores. Competition in soft goods business will naturally increase.

Lower volumes, together with price ceilings deliberately intended to squeeze margins, put pressure on costs and require curtailment of expenses and reduction of services. Naturally the pressure falls heaviest upon merchants who are less adaptable, less efficient, or less fortunate in the impact of the price regulations, than their competitors. Personnel problems will become more difficult as employes enter the armed forces or shift to war work. Short-

ages will be fewer and far less severe than in Great Britain, where the ranks of smaller shopkeepers have suffered heavy casualties as trade became smaller and more concentrated, but similar influences will be at work.

The situation is difficult for distributors of durable goods who are being forced out of business and for those who will be unable to survive the pressure on their operating margins. It must be understood, however, that this is part of the war effort and the inescapable cost of the war. If distribution can be carried out by fewer people, more will be available for war work. Consumers on their part will find how well they get along without all the accustomed services, and out of the wartime influences may come permanent economies and cost reductions in distribution.

Money and Banking

Treasury figures through June 26 indicate that the budget totals for the fiscal year ended June 30 were close to the revised estimates, which placed the net deficit at approximately $20 billions. The increase of more than $21 billions in public debt during the year was financed readily, at low rates of interest and with no demands on the banking system which could not be easily met. The June financing, apart from the weekly Treasury bill offerings, consisted of $1,500 millions certificates of indebtedness due February 1, 1943 and bearing ⅝ per cent interest. Subscriptions were twice the amount of the issue.

The new fiscal year opens with a sharply stepped-up program of borrowing. The Treasury has announced its intention to raise up to $4.5 billions of new money during July and August. As shown in detail in the tables in the June issue of this Letter, it is estimated that in fiscal 1943, after allowance for outlays by government agencies not included in the budget, and for net receipts from social security and other trust funds, the total of new securities to be sold to the public will be approximately $47 billions. Of this sum, the Treasury hopes to raise $12 billions through the sale of war savings bonds, while purchases by insurance companies, mutual savings banks and other investors (excluding commercial banks), plus net sales of tax anticipation notes, have been estimated at around $6 billions, based on a projection of recent trends. This would leave $29 billions of the new securities to be taken by the commercial banks.

How Banks Pay for Treasury Securities

Probably many people do not understand how the banks can possibly absorb such a stupendous amount of Treasury securities. The explanation, of course, is that when the banks subscribe to government securities and pay for them by making bank deposits available to the Treasury, such deposits, after they have been collected into the Treasury account, are disbursed for wages, materials, etc. Thus they return quite promptly to the banking system and remain there. This does not mean that the new deposits necessarily remain with the same banks where they originated, but merely that for the banking system as a whole there is no loss of deposits.

Inasmuch as the banks generally do not use cash, but credit, for payment of their subscriptions to new government issues, it is apparent that the process can go on so long as the banks have unemployed or excess reserves to satisfy the legal requirement for reserves against the additional deposits created by these subscriptions.

At the present time the excess reserves of all member banks amount to approximately $2.6 billions. If the estimate given above that the commercial banks will purchase nearly $30 billions of new securities during the coming fiscal year is realized, the purchases will cause an equal expansion in deposits. Assuming the expansion to be wholly in demand deposits, and calling for an average of reserve requirements for the country as a whole of 20 per cent, this would mean an increase of about $6 billions in required reserve, or more than twice the amount of the present excess. To the extent that money in circulation continues to expand, there would be a corresponding drain on the total of bank reserves held.

Additional bank reserves to meet the drain may be provided in a number of different ways, of which one—open-market operations by the Federal Reserve Banks — has already been started. The Reserve Banks recently resumed adding to their holdings of government securities, and between April 8 and June 24 increased them $340 millions. These purchases increase member bank reserves by an equal amount.

A second means of easing the reserve position of member banks would be through exercising the powers of the Federal Reserve Board to lower the percentage of reserve required to be held against deposits. A bill now before Congress would give the Board greater flexibility in the exercise of these powers so that they may change requirements for central reserve city banks independently from reserve city banks or country banks, all within the present limits of the law.

In these and other ways available reserves can be increased by action of the monetary authorities. Finally, if necessary or desirable, member banks can borrow from the Reserve Banks. These banks have the power to supply credit beyond any prospective needs, for their enormous gold certificate holdings, representing the bulk of the country's monetary gold stock of more than $22 billions, are available

as reserve upon which they can expand their own deposit and note liabilities.

Distribution of Bank Deposits and Reserves

Total deposits of all member banks increased by $10 billions or 19 per cent from the beginning of the expanded defense program in June 1940 to April 1942. The uneven distribution of this increase is shown in the accompanying table, giving the percentage changes by districts and by classes of banks to the latest date for which such details are available.

Percentage Change in Total Deposits and Reserve Position of All Member Banks, June 1940 to April 1942

Total Deposits By Districts	Cen. Res. Cities	Reserve Cities	Country Banks	Total
1. Boston		+12	+21	+17
2. New York	+11	+17	+20	+12
3. Philadelphia		+14	+10	+12
4. Cleveland		+22	+24	+23
5. Richmond		+30	+36	+33
6. Atlanta		+29	+40	+34
7. Chicago	+17	+37	+29	+26
8. St. Louis		+34	+33	+34
9. Minneapolis		+16	+14	+15
10. Kansas City		+24	+25	+24
11. Dallas		+27	+30	+29
12. San Francisco		+22	+26	+23
Total	+12	+24	+24	+19
All Member Banks, Reserve Position				
Held reserves	—24	+16	+25	— 7
Required reserves	+28	+55	+62	+41
Excess reserves	—74	—31	—16	—56

It will be seen that the gains in bank deposits by districts ranged from Atlanta and St. Louis with 34 per cent to New York and Philadelphia with 12 per cent. In New York City the increase was but 11 per cent, against 17 per cent for the reserve city banks in this district and 20 per cent for the "country" (other) banks. For the system as a whole, the gain in the two central reserve cities of New York and Chicago was but 12 per cent, against gains of 24 per cent for the reserve city banks and the same for country banks.

Corresponding figures in the table as to reserve position show that excess reserves of central reserve city banks were cut by 74 per cent during the period, compared with decreases of 31 per cent for the reserve city banks and but 16 per cent for country banks. Of the decline in excess reserve of all member banks from $6.8 billions in June 1940 to $2.6 billions at present, some 80 per cent has been in New York City, where the drop has been from $3.7 billions to $485 millions.

The reason for this flow of reserve money out of New York is to be found chiefly in Treasury operations. The Treasury regularly collects a substantial part of its total tax funds in New York and sells in New York a disproportionately large share of government securities. The funds withdrawn from New York in this way are spent in war time all over the country, and particularly in areas where war production or military operations call for large disbursements. The net result is a tendency for funds to move out of New York to other parts of the country.

Support for New York Money Market

Thus, as the huge program of war finance goes forward, the first impact is felt in the New York money market. So far this impact has been adequately cushioned by existing excess reserves and by funds supplied by the Federal Reserve Banks through purchases of government securities in the New York market; and the New York banks have recognized the problem and have undertaken to give full support to the Treasury financing program by using their reserves more fully.

While short money rates have firmed slightly from the fractional figures of two years ago, there has been no serious disturbance of the money market or the government security markets, and the whole financing program has been moving smoothly. The slightly higher rates are in fact helpful in attracting buyers other than banks. It is a fair assumption that the Treasury and the Federal Reserve Banks will keep the banks of the country, both in New York City and in other areas, supplied with the necessary reserve funds for the financing program, and that, with the cooperation of the banks, even this huge program can be carried through without any serious mechanical difficulties.

The real problem of government financing lies, not in the mechanics, but in the general effect on the country's economy of the huge expansion of bank credit. As has been repeatedly emphasized by Secretary Morgenthau and other government officials, and as discussed frequently in these columns, every effort must be made to finance the war program as fully as possible out of the current income of the people. Only if people save and buy bonds can the dangers of inflation inherent in this huge operation be kept at a minimum.

Latin America Faces New Economic Problems

The economic problems which the war has created for the Latin American countries have taken on new aspects during recent months. When the Pan-American Conference met in Havana two years ago, after the fall of France, the subject uppermost in economic discussion was the loss of European markets and the danger of trade depression. Since the Latin American republics normally export 30 to 50 per cent of their production, and almost a third of their sales went to the Continent of Europe, it was natural to fear that collapse of this trade would leave them with unsold surpluses, depressed markets, and spreading economic distress.

Fortunately these fears proved to be over-pessimistic. Within a few months following

the Conference, purchases of Latin American products by the United States, then embarking on the defense program, expanded to such size that they not only absorbed surpluses of some of the vital export commodities, but actually lifted the greater part of Latin American production above the pre-war level. By September 1941, the last month for which detailed trade figures were published, our purchases from Latin American countries were at the annual rate of about one billion dollars, and they are probably higher now. At that level they were nearly twice as large as in 1939, and the increase practically made up for Latin America's lost trade with the Continent, which had averaged about $500,000,000 in 1938 and 1939.

Furthermore, business in some of the republics was supported by a substantial inflow of foreign funds. From the beginning of the war there has been a considerable flow of refugee capital from Europe, and some Latin American capital was repatriated from the United States in the course of 1941. New money was supplied by Export-Import Bank loans, although these have been much smaller than most uninformed people suppose. Finally, much of the money formerly spent abroad by wealthy Latin Americans or sent abroad by immigrants is now retained at home. The Review of the River Plate makes the following comment:

> The enormous amount of money which used to be spent abroad is now being spent at home, and this discovery of Argentina by the Argentines will have permanent effects, since the return of the prodigals has made notable difference in social customs, habits of dress and manners of recreation and collective enjoyment.

With the benefit of these developments, and with internal measures supporting agriculture against loss of export markets, Latin American countries have made a striking recovery from the 1940 depression. Their currencies have strengthened in the exchanges, dollar balances have been built up, and some repatriation of foreign debt and conversion of internal debt has been accomplished. With few exceptions, 1941 was the best year since 1929; and although 1942 has brought the necessity for new adjustments, and for wise guidance of economic trends, it also is certain to be a year of high activity.

New Trade Interferences

Present economic problems which confront the Latin American nations arise largely from the entry of the United States into the war. One of the problems is to deal with fresh shifts and dislocations in their trade caused by wartime restrictions on United States exports and imports, and by the disruption of shipping by submarine warfare in the last few months. The second is to control the inflationary forces which have been set in operation by expanding purchasing power, at a time when many goods for which Latin America now depends on the United States can no longer be obtained.

Obviously these two problems are associated. As long as the increase in sales within the Western Hemisphere results in well balanced trade and in increased production and consumption, it is a source of genuine prosperity. A difficulty in the present situation, however, especially since shipping scarcity became acute, is that United States purchases are concentrated heavily in the strategic materials. On the one hand the Latin American countries are experiencing a boom in these materials; on the other, our purchases of certain consumption goods have fallen considerably below 1941 levels, and surpluses of these goods are accumulating at the ports. At the same time our priorities, restrictions on consumer goods production, and export quotas have interfered more and more with our exports, and although Latin American countries have the means to pay and are eager to buy more manufactured goods, fuel and certain raw materials, we cannot satisfy the demand.

The result is that dollar balances of the Latin American countries are accumulating. Their export surplus (including gold and silver) to the United States, which exceeded $200 millions in 1941, is estimated by some authorities at $500 millions this year. Meanwhile Latin American producers have an expanded purchasing power, both through their exports and through government purchases, loans or subsidies. Credit is expanding, speculation has developed in some areas, and the rise in prices of manufactured products has been accelerated. This is the inflationary problem.

The Inflationary Danger

Argentina is one of the countries particularly affected, and the situation is described with great clarity in the recently issued annual report of the Central Bank of the Argentine Republic. Referring to "the negotiation in Washington towards the end of 1940 of financial operations for a total of $110 millions," the report proceeds:

> The exchange was to serve for the payment of essential imports which it was not advisable to restrict severely, and the equivalent amount in pesos obtained from the sale of that exchange was to be used chiefly to finance the purchase of the crops without resorting to an internal expansion of banking credit.
>
> However, circumstances have changed to a remarkable degree since then. Our exports to the United States have shown a very marked improvement rising from a total value of 264 million pesos in 1940 to 562 million pesos in 1941. In addition, the country has received an appreciable quantity of exchange through the inflow of foreign funds. The balance of payments, instead of becoming increasingly unfavorable as had seemed likely at that time, now shows a credit balance. In the present circumstances, therefore, there is no shortage of exchange. But, unfortunately, another and far more serious problem confronts us, we have sufficient exchange available but there is a shortage both of goods and of ships to carry them . . .
>
> The problems of exchange and of loans have now become secondary ones. Additional exchange would be of very little use in the present circumstances—

> except for the building up of reserves for the future — while it cannot be employed to obtain the essential imports which the country needs . . .
>
> We are passing through an exceptional moment and our reactions must of necessity be different from those which were justified by the conditions prevailing formerly. The entry into this country of exchange or foreign funds which cannot be used for the purchase of the foreign goods which the country needs may give rise to problems similar to those posed by the internal creation of additional quantities of purchasing power without the safety valve of imports.

Expansion of Credit

The report also comments on the expansion of bank credit "because the Government has made extensive use of the resources of the banking system to purchase surplus crops and finance expenditure which cannot be covered by the customary means at the command of the Treasury." This refers to corn principally, also wheat and flaxseed, exports of which have been continuously depressed ever since the loss of Continental markets. Bank credit expansion naturally has been called for on other grounds also, by increased production of strategic materials, trade expansion and higher prices; and it is a problem of all countries. As will be seen from the following table, commercial bank deposits in Brazil, Peru and Mexico about doubled in the past four years:

Commercial Bank Deposits in Latin America

(In Millions of National Currency)

End of	Argentina	Brazil	Chile (a)	Colombia (b)	Mexico	Peru (c)
1937	3,881	8,812	1,911	89	273	254
1938	3,791	11,665	1,923	96	275	287
1939	3,913	12,523	2,049	116	351	318
1940	3,940	13,714	2,152	132	490	401
1941						
March..	4,156	14,541	2,275	146	544	405
June	4,351	15,133	2,383	154	577	416
Sept. ..	4,453	16,055	2,584	154	602	462
Dec.	4,585	16,532	2,468	146	586	448
1942						
Feb.	4,750		2,466	155	619	
March..	4,780		2,533		630	

(a) Including government deposits. (b) Including mortgage and savings banks. (c) Including the Savings Bank of Lima.

As long as there is room to expand industrial activity, either within existing capacity or by increasing capacity, proportionate increases in bank credit are not inflationary. The inability to buy abroad, however, restricts industrial activity and capacity to expand. The report of the Argentine Central Bank goes on to say:

> To continue creating demand beyond those limits by the increase of purchasing power of internal or foreign origin would entail very serious and ever growing complications. The trend of these factors will, therefore, have to be carefully watched so that dangerous excesses may be checked in time.

Scarcity of Imported Goods and Rising Prices

Shortage of imported goods has been most serious in Argentina, Brazil and Uruguay, where even last year irregular deliveries of fuel interfered with local industrial activity. More recently the shortage of steel, non-ferrous metals and industrial equipment has slowed down new construction as well as factory operations. Many new projects, including public works, have had to be postponed.

To allocate imported goods and keep prices down, a majority of the Latin American countries have introduced various trade controls and price fixing measures. Nevertheless, the price movement in many quarters remains uncurbed. In Argentina, for example, certain imported products have been reported selling at prices ranging as high as 500 per cent above the U. S. ceilings for such goods. Wholesale price indexes, wherever they are available, show an accelerated rise, confined principally to imported and manufactured products. This is shown in the following table:

Trend of Wholesale Prices in Latin America

(1937-39 = 100)

Date	Argentina Agri.	Argentina Other	Peru Expt.	Peru Impt.	Chile	Mexico
1937-39	100	100	100	100	100	100
1940	86	119	107	134	106	103
1941						
Mar.	78	126	108	147	110	104
June	82	138	111	161	119	109
Sept.	84	160	121	180	133	114
Dec.	85	172	133	192	147	114
1942						
Jan.	86	178	130	200	152	115
Feb.	86	181			153	116
Mar.	86	183				117

With living costs rising, agricultural and industrial workers in a number of countries have been pressing for higher wages. As a result costs of domestic manufactures have also been advancing. On the other hand, with the commodities not essential for war effort accumulating on the docks and export prices kept down, producers in rural areas are bound to have a smaller real purchasing power except as their situation is supported by government measures.

Commodity Surpluses

Effects of reduced United States purchases of some of the staple Latin American products have varied from country to country. In some they have not assumed dominant importance, and commercial activity has continued unabated at levels above last year. In the Caribbean countries business has remained good despite considerable falling off in shipments of sugar and bananas.

The accumulation of exportable products has had more unfavorable consequences in South American rural districts. In Argentina in particular the 1941 trade revival did little to relieve the situation in respect to burdensome stocks of corn. Now wool stocks have been accumulating in Argentina, Uruguay and Chile because of the lack of bottoms. Coffee and cocoa shipments from Brazil have declined considerably in the last few months. The table on the next page gives the latest available figures for certain leading export commodities.

Latin American Exports of Important Commodities, by Countries

Commodity	Period	Unit	1940	1941	1942
Sugar					
Cuba	Jan.-June 20	000 long tons	1,268	1,489	919
Puerto Rico*	Jan.-June 20	000 long "	313	408	300
Coffee					
Colombia	Jan.-May	000 bags	1,545	1,570	1,801
Brazil	Jan.-May	000 "	5,757	8,438	4,298
Cotton					
Brazil	Dec.-Feb.	000 bales	139	363	116
Peru	Jan.-March	000 "	67	94	30
Cattle Hides					
Argentina	Jan.-April	000 m. tons	50.2	44.6	43.9
Wool					
Argentina	Oct.-April	000,000 lbs.	239	291	158
Uruguay	Oct.-May	000,000 "	88	117	46
Flaxseed					
Argentina	Jan.-April	000,000 bu.	20.3	5.0	6.3
Wheat					
Argentina	Dec.-April	000,000 bu.	67	34	33
Corn					
Argentina	Jan.-April	000,000 bu.	37	10	2
Bananas					
Costa Rica	Jan.-March	000 stems	705	723	470
Panama	Jan.-March	000 "		2,022	676

*Receipts of Puerto Rican sugar at U. S. ports.

This table shows the improvement in commodity exports in 1941 over 1940, except in the case of the Argentine commodities mentioned. It also shows the decline in shipments in 1942 as compared with 1941, affecting most of the commodities.

Despite depressed grain exports, total value of Argentine exports for the first four months of 1942 was still 30 per cent higher than in the same period last year, the gain reflecting generally higher prices and heavier movement of meat products. Brazilian exports for the first two months of 1942 were 50 per cent ahead of last year; this was due in part to higher prices and in part to a remarkable diversification of exports. The share of coffee dropped to 37 per cent, from about 45 per cent in 1938, and for the first time cotton textiles occupied second place. The value of mineral exports quadrupled between 1939 and 1941, reaching almost $30,000,000 last year, and has shown a further sharp rise during the first two months of 1942.

Permanent Gains

All analyses of the economic problems of the Latin American countries have agreed upon the lasting benefits to be gained from a sound growth of industrialization, diversification of agricultural and mineral production, and increase in trade among the countries themselves. Along each of these lines progress has been made during the past two years, and is continuing, in some quarters with United States technical and financial aid. It is possible that some new developments may prove to have been based on war demands and inflationary influences rather than upon a secure foundation of efficiency and low cost, but in the aggregate industrialization is a permanent gain, which will result in increased consumption and living standards. In Argentina the promotion of new joint stock companies in 1941 is said to have broken all previous records. Locally made consumers' goods, ranging in variety from canned food products to clothing, shoes and textiles, are replacing imports on an increasing scale. In Brazil cotton and rayon mills furnish not only the bulk of domestic needs but do considerable exporting.

Heavy industry development is also proceeding. Argentina, after gradual growth over a period of years, is now able to supply a part of her requirements of dyestuffs, refrigerators, electric motors, porcelain and special glass with domestic products. In Brazil a new steel mill, financed in part by the Export-Import Bank, is under construction which will eventually bring the country's capacity to over 1,000,000 tons.

Growth of trade within Latin America has helped business recovery and puts it on a sounder and broader basis. The dollar value of the trade of Argentina, Brazil and Chile with each other and with other South American countries reached about $270,000,000 in 1941 compared with $170,000,000 in 1938. A number of trade agreements on the most-favored-nation basis have been made, and several regional conferences have been held with the purpose of fostering the flow of trade and lowering trade barriers. The trade treaty between Argentina and Brazil, signed last November, is intended to establish a "progressive customs union" by providing free entry over a period of ten years to goods produced by any new industries in either country.

The United States has both a sympathetic and practical interest in the Latin American problems. The effect of the loss of Far Eastern raw materials is to tie this country even more closely than before with Latin America, but of course our interests go far beyond the search for products which were formerly imported from Southeastern Asia. Latin American bases and suppression of Axis movements are essential to their and our security. Ten of the Latin American countries have joined us in the declaration of war, and virtually all are contributing to the common security in one way or another.

The United States has its own problems. It is short of the capital goods and equipment as well as the consumer goods which the Latin American countries want, and cannot protect Latin America, any more than itself, entirely from the economic consequences of the war. This is recognized below the border; and most countries have taken steps to conserve fuel and essential manufactures. The responsibility of all the countries is to share scarce goods and raw materials in the proportions that will best serve the war effort.

There is discussion of plans whereby the United States will purchase various raw materials for storage in some of the Latin American countries until cargo space is available, as the British have done in West Africa and Australia. An arrangement has already been made to purchase cotton from Peru for temporary storage in that country. As to meeting Latin American requirements for goods, the United States and the Southern countries are cooperating in surveys of essential needs, in allocations of supplies, and in control of the ultimate use of what we can ship. A possibility is shipment of machinery for producing consumers' goods, now rendered idle here, to those countries where necessary raw materials are available.

Obviously there is no overall or quick and easy solution to the present problems. They require patience and mutual sympathetic effort. As the Argentine Central Bank said, problems of exchange and of loans have now become secondary to problems of distribution of goods.

Food For the War

There has been no revival in 1941-42 of the slogan of 1917-18, "Food Will Win the War", but it is as true now as it was then that an increased agricultural effort and production are called for imperatively. Farmers have the task not only of feeding our own population, but of supplying the heavier per capita needs of the armed forces, making up where possible for deficits in food imports, and providing vast supplies for our Allies, — all while the farms are yielding thousands of able workers to the Army and Navy and thousands more to the war industries.

Moreover, the war requires shifts in farm programs. The war demand is for concentrated foodstuffs. This means producing more of the oil crops and livestock, dairy and poultry products, which are rich in concentrated proteins. Greater quantities of fruits and vegetables are needed. At the same time the supply of feeds necessary to support the larger output of animal products must be maintained. On the other hand, the country can do with a smaller wheat acreage, since wheat supplies are burdensome and the surplus will be raised to new record heights by the heavy yield in prospect this year.

Even after the defense program was well under way, few people foresaw the demand for foodstuffs that would fall on American farmers; but fortunately Secretary Wickard and his advisers in the Department of Agriculture were among the far-sighted. He called for more hog production as far back as December 1940, although hogs were then in surplus supply, the price was down to $6, and the Lend-Lease program had hardly been conceived. From that time on, successive increases have had to be made in food production goals, just as in the goals for planes, ships and tanks.

Purchases of farm products for Lend-Lease have been on a steadily ascending scale. In April this year they reached $194 millions, nearly double the previous peak in March and nearly three times the average monthly rate during the program's first year. Total purchases to May 1, 1942 were $1,071 millions. Deliveries during the same period were $651 millions. The difference represents an accumulated stockpile out of which steady and probably increasing shipments of foodstuffs will be made. Of all Lend-Lease purchases, meat, dairy and egg products account for about one-half, and fruits and vegetables close to one-third.

Farmers Meeting Production Goals

The response of the farmers to the war needs has matched the response of the industries, and the farm effort has been favored by banner pasture conditions and crop prospects. The June 1 government crop report said that if the weather continues favorable all records for agricultural output may be broken by a considerable margin. In any case, farmers will turn out by far the greatest volume of animal products and vegetable oils on record.

Hog slaughter over the next few months is expected to run 15 to 20 per cent greater than a year ago; and with an indicated 25 per cent increase in the 1942 Spring pig crop, slaughter facilities next Winter will be taxed to capacity. The Department of Agriculture foresees the possibility of a slaughter peak around 7.5 to 8.0 million head for next December or January, well above the all-time record of 6,600,000 in December 1924, and is urging farmers to spread their marketings more evenly than usual. Some 83,000,000 hogs are expected to be slaughtered in this calendar year; and in the statistical year Oct. 1, 1942 - Sept. 30, 1943, the number may exceed 100,000,000. These totals are far above all past records.

So far as total meat production is concerned (pork, beef and lamb), it now appears likely that the Department of Agriculture's 1942 calendar year goal of 21,750,000,000 lbs. will be reached, and that 1943 production will be even larger. Total meat production in 1941, the largest on record, was 19,506,000,000 lbs.

All-time production records are being set in milk, dairy and poultry products. Egg production has been running 16 per cent above a year ago, comfortably above the 13 per cent increase asked for. While the gain in milk production so far has only been about half what the goals called for, production of cheese and evaporated milk has exceeded the goals by a wide margin. The Department of Agriculture early in the Spring raised its buying price for butter to switch milk from the condensaries back to the creameries, and within the past month has called for a reduction in evaporated milk output. Secretary Wickard now is urging people to eat

more cheese. A year ago he was calling for curtailment in consumption. Meanwhile cold storage stocks of cheese have doubled and evaporated milk stocks (including government holdings) are six times as large.

Supporting the prospect for animal products is a satisfactory feed situation. It was the country's good fortune to enter this year with record stocks of feed grains. The 1942 barley and rye crops are estimated to be much larger and oats slightly larger than last year. While it is too early to estimate the late-planted crops, corn is off to a good start and the increase in acreage appears fully up to the goals. The supply of concentrated feedstuffs probably will be 25 per cent larger than last year due to the heavy production of oilcake in prospect. The number of livestock to be fed will be a record, but if final crop yields are up to average, feedstuff supplies per animal for 1942-43 should be somewhat above average, although probably 10 per cent smaller than during the season now drawing to a close.

Fats and Oils

Along with the big rise in lard production — to be devoted to Lend-Lease purposes — the increase in domestic oilseed crops will be huge. The Japanese conquest of the Philippines and the Dutch East Indies suddenly cut off this country from the sources of two-thirds of its usual imports of vegetable oils. At the same time we were confronted with increased demands for fats and oils from Great Britain, Canada and Russia, which normally drew much larger supplies from the southwest Pacific area than did the United States. Both in this country and Great Britain, fats and oils have come to be a far more important source of food energy than during the last war. Per capita consumption here has increased over 50 per cent since 1912 and now provides us with some 25 per cent of our food energy, while before the present war some 35 per cent of Great Britain's caloric food requirements were obtained from fats and oils.

New and substantially larger fats and oils goals were set up within a month after Pearl Harbor. Farmers were asked to increase their soybean acreage 54 per cent, flaxseed 31 per cent and peanuts 155 per cent. From present indications the soybean and flaxseed goals will be reached, although the peanut goal has proved to be unattainable this year.

On the basis of present prospects for the oil crops and livestock slaughter, it appears that production of fats and oils in 1942 will show an increase of around 1,000,000,000 pounds over 1941 production of 9,300,000,000, with another increase of 1,000,000,000 pounds or more likely in 1943. However, domestic consumption this year, if unrestrained, may equal or exceed last year's record of 11,000,000,000 pounds. Imports are likely to be only half what they were in 1941, and a much smaller proportion will be edible. Exports, principally lard, will exceed total imports if shipping is available. Hence domestic production this year hardly can be expected to cover domestic demands fully, and the drain on stocks will be substantial. It is too early to say whether limitations on consumption will prove necessary. Naturally the situation will vary as between the different oils, but there is a high degree of interchangeability among them.

The Problems Ahead

So far as domestic food growers can provide, therefore, overall food supplies promise to be abundant for home use and for as generous provision for our Allies as shipping facilities permit. Nevertheless, there is no room for complacence or for relaxation of effort. Some foods will be scarce, and problems of distribution will be far more complex than in normal times. Secretary Wickard in a recent speech delivered in New York before the Grocery Manufacturers of America described the food outlook as follows:

> A year ago it seemed certain that we could meet all foreseeable lend-lease needs and have plenty of all kinds of food for all other uses, and even some to spare. Of course, it looked as if farmers would have to produce more of some things, and processors handle more. But generally speaking it seemed that the normal methods of producing, processing, and distributing food could go on as usual.
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> That is not true any longer. Already we are actually sending our Allies a lot more food than we thought we would a year ago, and we will send them even more as soon as more ships are available. It is still safe to say that everyone in this country can have enough nourishing food, but we can't be certain that we won't run short of some particular kinds of food and have to make up the lack with other kinds of food. And it's already a certainty that many kinds of food will reach consumers in different packages or different forms from those they are used to, and that many methods of distribution will have to be changed.

Lack of shipping is reducing current receipts of most imported foodstuffs substantially below normal consumption. In addition to the sugar rationing, limitations have been placed on the wholesale distribution of coffee, tea and cocoa. Much of the canned fish pack, including all the Pacific coast tuna and salmon, is being taken by the armed forces, and government and Lease-Lend purchases of canned fruits and vegetables will cut heavily into the supply. If improvement in the shipping situation permits greater food imports, it will also make possible greater exports, and both Great Britain and Russia could use more food than they are receiving.

Even though the basic food crops continue to develop satisfactorily until harvest time, the battle to supply war needs will be won only when they have been harvested, stored, processed, and transported to the places where they will be needed and in the proper form. Some of the more apparent problems, in addi-

tion to shipping, include prospects of labor shortages in certain areas at harvest time; scarcity of storage space, particularly in the wheat belt; the ever increasing burdens being placed on the railroads; growing shortages of materials needed in the processing and packaging of foodstuffs.

More will be heard of the need for harvest labor as the season progresses, and Government authorities are already recruiting workers from the cities. In the wheat belt the Government is contracting for erection of wooden storage bins having a capacity of 100,000,000 bushels, and another 40,000,000 bushels will be stored in steel bins transferred from the corn belt. Railroads will enforce stricter limitations on movement of wheat to congested terminal markets than ever before. Secretary Wickard has indicated that a permit system may have to be invoked next Winter to control the marketing of hogs if slaughter facilities of packers are not to be over-taxed.

Saving Shipping Through Dehydration

The scarcity in ocean tonnage is being reflected in greater emphasis on the saving of shipping space through dehydration, which evidently will outlive the war. Trade sources state that between forty and fifty dehydrated foods will soon be on offer to domestic consumers. Lend-Lease requirements for evaporated milk have been cut to only one-third of the original goals, and producers are being urged to increase their production of powdered milk which requires only about one-fourth the shipping space. Egg drying plants are being expanded to an annual capacity of 240,000,000 pounds compared with a 1941 production of over 45,000,000 pounds, which was six times the 1940 output. The meat packing industry is developing new dehydration processes for reducing beef and pork to 55 per cent pure protein; but before large scale operations can be started, allocation of critical materials must first be secured. Food packaging is changing considerably. The canning industry is cutting its consumption of tin by half or more through use of substitute containers (glass, blackplate and paper), and by using cans with thinner tin coatings.

Secretary Wickard is optimistic that most of these problems can be met through proper planning and coordination of effort. During the past month a Food Requirements Committee, headed by the Secretary, has been created within the War Production Board; and a Combined Food Board has been jointly established by the United States and Great Britain, for the purpose of anticipating and meeting all food needs.

One of Mr. Wickard's problems, in which his position has the full support of President Roosevelt, is to hold prices of feedstuffs at levels which leave an attractive margin between feed costs and prices of animal products, and therefore provide an inducement to expand livestock, dairy and poultry production. Through the sale of surplus corn and feed-wheat from the holdings of the Commodity Credit Corporation at 85 per cent of corn parity (the farmer receiving parity through loans, soil conservation and price adjustment payments), feed prices have been kept at the desired levels.

However, the House of Representatives wants to prevent the sale of any government owned commodities below the full parity price, with the exception that deteriorated wheat may be sold at prices competitive with corn. Mr. Wickard met this proposal by suggesting that sales of wheat for feeding purposes be limited to 125,000,000 bushels, at prices not below 85 per cent of the corn parity price. The Senate accepted this suggestion, incorporating it in an amendment to the 1943 appropriation bill, but the House voted down the amendment. Meanwhile bills have been introduced in both the House and Senate to require government loans on basic crops (wheat, corn, cotton, rice, peanuts and tobacco) at 100 per cent of parity, instead of 85 per cent as now provided.

If corn prices are forced up to full parity either feeding margins will be narrowed, or prices of animal products must rise. In the first case the incentive to production would be diminished, while in the second the consumer would pay the bill, the cost of living would be raised, and the inflationary forces augmented. At this writing the Conference Committee is deadlocked. In view of the requirements of the war food program it is plainly in the general interest that the Senate should hold to its position.

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